RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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**Aug. 17, 1994** **LETTER 1154**

**THE PICTURE:** I spend an hour or two every day listening to the comments of advisors and assorted "experts" on TV. Frankly, I give very little credence to these comments. But I listen mainly to get a handle on the psychology of the moment. Almost without exception, the commentators talk about "what has to happen" for the market to do this or that. For instance, if employment picks up the market should go up, or if the Fed raises the rates the market will slide, or if a health bill is passed the market will rally. Worthless guesses based on possible coming events.

What I do note is that almost no one talks about the primary trend of the market being SET. In other words, none of the commentators are now talking in terms of the inevitability of a major and long-lasting decline, a decline based on the fact that the tide has turned down and we're in a primary bear market. These advisors don't think that way; they don't recognize or understand the inevitability of the action during a bull or a bear market. They still think in terms of events, of what event might turn the market up, of what might happen if Clinton's approval rating goes up or down, etc.

This mistaken way of thinking is the main reason why people don't get into bull markets until the bull market has traveled a long way on the upside -- these people won't move until they hear the actual good news (which comes much later). In other words, they just don't understand the meaning of a primary bull trend. It also explains why people won't exit from a bear market until they've been literally knocked out of their investments -- they'll sit tight until they hear the actual bad news (which comes much later). Here too, they just don't understand the meaning of a primary bear trend.

**CORRECTIONS:** Every movement in the stock market, whether major, secondary or minor -- is ultimately corrected. When this happens neophytes are usually surprised -- often amazed.

Probably the most shocking and unexpected correction in stock market annals occurred following the great crash of 1929. The Dow topped out on September 3, 1929, at 381.17. Next, the market collapsed in an historic series of crashes. By November 13, the Dow had fallen to 198.69, an incredible loss of 48% of its value in a little over two months.

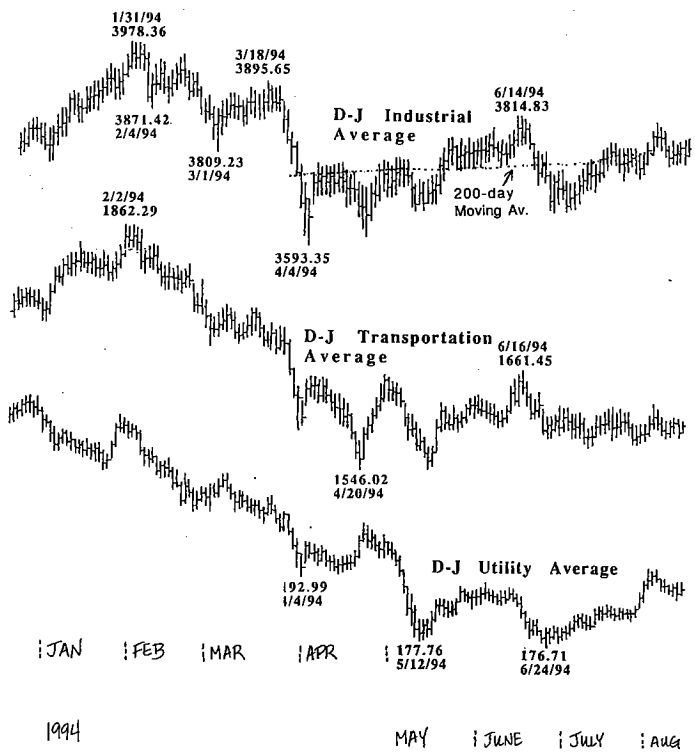
Following the November 13 low, stocks turned up and the corrective phase was on. The market climbed during December and all during early-1930. By April 17, the Dow had recovered all the way back to 294.07. Veteran Wall Street traders were in shock. Robert Rhea, the great Dow Theorist of the 1930s, wrote, *"Following the crash in '29 a secondary reaction in the bear market lifted the Dow to 294 in April 1930. This was a curious movement and a deceptive one. Doubtless it was influenced by the payment of a huge soldiers' bonus, the proceeds of which seems to have been spent largely for autos. I can remember having shorted stocks in early December, 1929, after completing a satisfactory short position in October. With the slow but steady advance of January and February, I became panicky and covered at considerable loss. With losses piling up every day, I forgot that the rally might be expected to retrace possibly 66% or more of the 1929 downswing. Nearly everyone was proclaiming a new bull market."* Russell comment: Secondary corrections can be expected to retrace one-third to two-thirds of the previous major advance or decline.

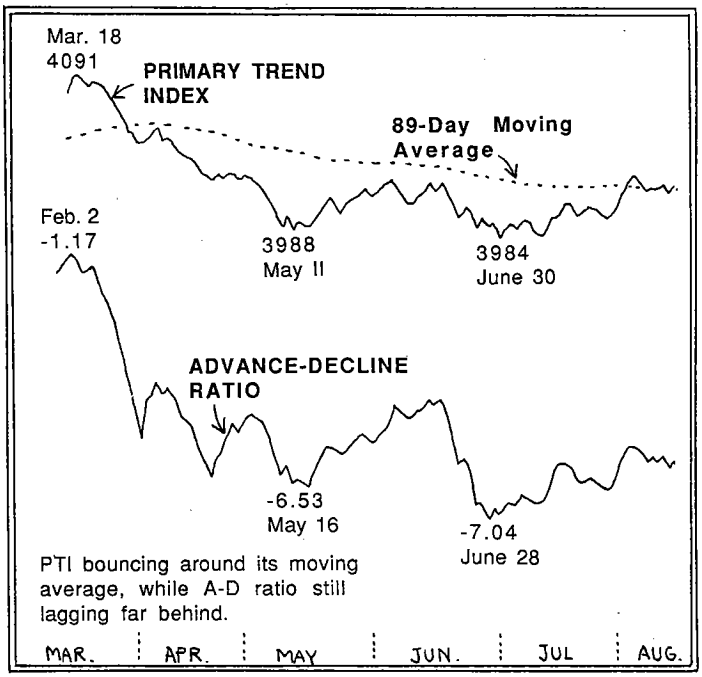
**Aug. 5 DJIA 3747.02; PTI 4012; A-D Ratio -6.13**
**Aug. 12 DJIA 3768.71; PTI 4018; A-D Ratio -6.11**
**Dow Yield: 2.70%; Dow Price/Earnings: 19.3**
**Dow 200-day MA: 3763; Dow 30-day MA: 3738**
**Dow Times Book Value: 3.37; PTI 89-day MA: 4014**
**Percentage of Undervalued Blue-chips: 12%**
**Dow Low Risk Buy Index: +12; Gold-PTI: 898**
**Gold 40-week MA: 383**

All right, now let's get into the present. The Dow hit its bull market high on January 31, 1994 at **3978.36.** The Dow then sold off, recording a low of **3593.35** on April 4. But the advance-decline ratio (a proxy for ALL the stocks on the NYSE) has performed considerably worse than the Dow. The A-D ratio recorded its high on February 2 at -1.17 and then turned down. The A-D slide continued to June 28 (the low was -7.04). *In other words, even though the Dow recorded its low on April 4, the majority of stocks, as measured by the A-D ratio, continued down for almost another three months -- until June 28.*

Thus, we witnessed an important *non-confirmation between price (i.e., the Averages) and breadth (i.e., the A-D ratio).* Downside price-breadth non-confirmations call for a reversal, and this one was no exception. The reversal started after June 28 (that was the day of the low for the A-D ratio). The Averages backed and filled for a few weeks, but on July 29 the market registered its first strong upside day. That was followed by a few days of further strength, and within a week bullish analysts were optimistically predicting "Dow 4200" by the end of the year.

In this business it doesn't pay to be stubborn. Stubborn on Wall Street is a synonym for stupid. And stupid on Wall Street is a sure formula for losing money. During the '60s the hippies' theme-song was, "Give love a chance." In my investing life I've developed a stock market theme-song of my own. It goes, "Give the market a chance."






What chance am I talking about? All right, we've had the market overvaluation (we still do), we've had the excitement and froth of the third phase of the bull market, we've had the craziness (we still do) of the public pouring billions of dollars daily into 5,000 assorted mutual funds. Then we had the Dow Theory bear market signal of March 27, 1994. And more recently we've had a rally. So now let's give the stock market "a chance" to prove itself one way or another.

What are we watching for? The first really impressive action on the upside would be the following: both Averages would better significant preceding peaks (refer to the page 1 chart). The first significant peaks are the mid-June highs of **3814.83** on the Dow and **1661.45** on the Transports. If the Averages manage to better those points the next important levels would obviously be the bull market highs of Dow **3978.36** and Transports **1862.29.** If both of those highs are bettered, the bull market would be reconfirmed and Richard Russell would have been wrong in labeling this a bear market.

Now let's look at the downside. On the downside we have the April bear market lows of Dow **3593.35** and Transports **1546.02.** If both of those lows are broken, I won't even have to report it -- you'll feel it, and you'll know it. And so will every stockholder and mutual fund manager in the nation.

By the way, turning to the Utility Average, this Average lost a very big 31% on the decline from its high in September 1993 to its April 12 low. Thus, a decent upside correction was almost obligatory. For this reason, I'll be particularly interested to see just how far the Utility Average can correct on the upside (so far, the Utility rally has not been impressive, having recouped only 16% of its losses). The action of the Utilities, although playing no part in classic Dow Theory, is always significant (if for no other reason than there is so much money involved in the action of dozens and dozens of utility stocks).

In the last Letter I referred to the divergence that was building between the Dow and the Transports in that the Transports were moving sideways while the Dow was working its way higher. This was obviously not a healthy development (study the page 1 chart).

I noted that the rally in the market was due mostly to an easing of selling pressure, rather than any impressive increase in buying. Rallies built on declining selling pressure (rather than a substantial increase in buying power) don't tend to last very long.

I also wrote that the market was "churning," as seen in the fact that the number of declines were tending to equal the number of advances -- even on days when the Dow was up strongly. Actually, I run a 25-day total of the differential between daily advances and declines. The 25-day total has been contracting into the "heavy churning" zone.

Finally, it should be noted that as the market rallies, the higher prices will increase the already lofty Dow price-to-dividend ratio. With Dow dividends now at 101.89 (actually down from a year ago), the current Dow price-dividend ratio is **37.** Historically, this is on the very high side. So clearly, any rally from here will simply put the Dow price-dividend ratio on even thinner and more dangerous ground than it is now.

Conclusion: Here's my overall view of the situation. This bear market promises to be a long one, a deceptive one (aren't they all) and ultimately a vicious one. I sense that very few people at this point really believe that we're in a bear market (not that they even know what a bear market looks like). And, of course, the bear loves it. Why? Because thousands of still-bullish investors will continue to put their money into stocks. And as I've said many times before, *the bear wants to take the market down with as many stockholders on board as possible.*

You also have to remember that the stock market is in no hurry. The market is never interested in "showing its hand," either to the bulls or the bears. Which is why I continue to emphasize patience. Wall Street has already been nice enough to provide us with a number of bear hints, some subtle and some not so subtle. But listen, it's early in the game, and I'm well aware that it could take until the fourth quarter or even into early 1995 before we start the second phase of this developing bear market.

The public has already taken some losses and many mutual funds are already down for the year -- most down only 3% to 10%, but they are down. Now we hear advisors telling people to "average down" if prices continue to decline. Averaging down is all right during a bull market correction. But averaging down early in a primary bear market is the ticket to disaster. Advisors who are now urging their clients to average down have, in all probability, never lived through a real, honest-to-God, primary bear market.

Perhaps most significant, *Wall Street, as it always does, takes the earliest hits from the bear.* You may not be aware of it, but the "Street" is beginning to perspire. And jobs are beginning to be lost. This AP article represents an early bear market warning.

*Worst Layoffs May Be Yet To Come*

## Blue Chips Down, Pink Slips Up — Market Malaise Trims Wall Street

By DAVID E. KALISH
*AP Business Writer*

NEW YORK — The ax is falling slowly on Wall Street, but it's falling.

Six months into a steep financial market decline, many of the nation's leading securities firms have laid off hundreds of traders, brokers and other employees to cut their losses in bonds and stocks.

work force of 435. The brokerage estimates the cuts will save it $60 million over the next year.

The outlook for the future is gloomy. Prudential Securities Inc. plans to cut up to 500 of its 18,000 workers by yearend — mainly support staff such as accountants and clerks — according to a company executive who spoke on condition of anonymity.

**INVESTMENT POSITION:** Please re-read the first section of page 1. Why? Because it's crucial to understand the inevitability concept regarding bull or bear markets. The bear is now in the box. If I'm correct in that this is the very early phase of a primary bear market (and I believe I am) then nothing -- no presidential edict, no Congressional bill, no Fed manipulation -- will save the stock market.

If it's a bear market, then one way or another, it's going to go down. Our job is to let it go down without us. Frankly, that's why I put the actual picture of the bear in the box. I feel that ugly bear puts me on the line. No waffling, no "ifs" or "maybes," the bear is in the box. Russell has put his big mouth and his fanny on the line.

But what if I'm wrong? Hey, if the Averages rally to new highs, I'll be wrong, wrong, wrong. But that hasn't happened yet -- despite the fact that there's plenty of good news and plenty of optimism around. Face it, this market is marching to the beat of a different drummer, and it's not the drummer that we read about in the newspapers.

Today we're being almost overwhelmed with investment advice. Magazines, newspapers, TV, radio, brokerage handouts, computers. And almost all of it aimed at telling us what funds or what stocks to buy. Under the spell of this "buy, buy, buy" barrage, it's hard to sit in cash and ignore the noise. But that's the plan. Would it be easier if we turned it into a game? All right, let's call our little game, "Making money by not losing it."

**MOVING AVERAGES:** One of the oldest methods in technical analysis is the study of moving averages (MA). Basically, a moving average simply smoothes the action of an item. Over the years various forms of the moving average have been utilized.

One study that I've followed for years (make that decades) is the juxtaposition of two moving averages, the time-honored 200-day moving average and the shorter 30-day moving average. Of course, with the advent of computers this study becomes a good deal easier to follow.

For years I've included the figures for the 200-day and the 30-day MAs of the Dow on the first page of this Letter. Most readers have probably ignored the figures, but the MA studies have more meaning when you can see them in chart form.

On the first chart we see the Dow (daily) and two MAs, the 200-day and the 30-day. Note that even though the Dow topped out in late-January, the 200-day MA is still rising. Obviously, the Dow has not held below the 200-day MA long enough to turn this long-term MA down. However, the rate of ascent is now declining. If and when the 200-day MA turns down, that will be a definite major negative for the market.

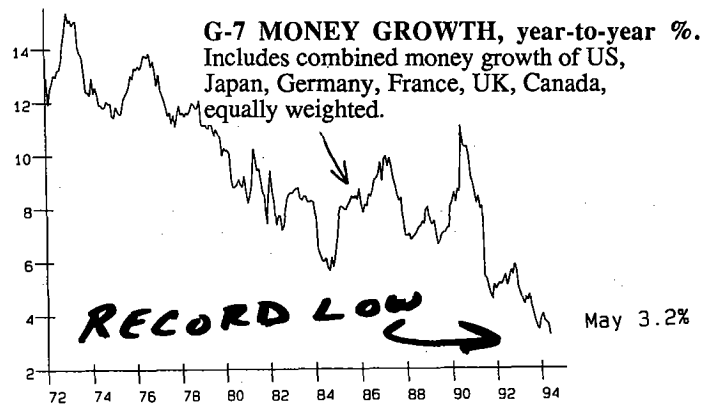
The position of the 30-day MA in relation to the 200-day MA is also very important. So far, we have not seen the true bear market relationship of these two. This would entail the 200-day MA declining, and at the same time the 30-day MA holding persistently below the 200-day MA. As this is written, the 30-day MA is below the 200-day MA, but as noted, the 200-day MA has not yet turned down.

Thus, there is still some upward momentum left in the Dow, but once the 200-day MA turns down it will be a signal that the upward momentum is exhausted, and the bear is beginning to have his way.

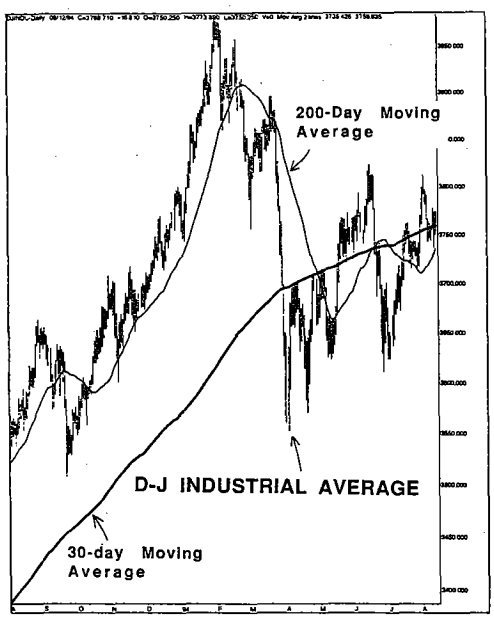
The second chart shows a somewhat different story. Here we see the much broader S&P 500 Composite with the two MAs, but note that here the 200-day MA has turned down. And the 30-day MA is holding well below the 200-day MA -- so on the S&P composite we're seeing the classic bear market position from the MA standpoint.

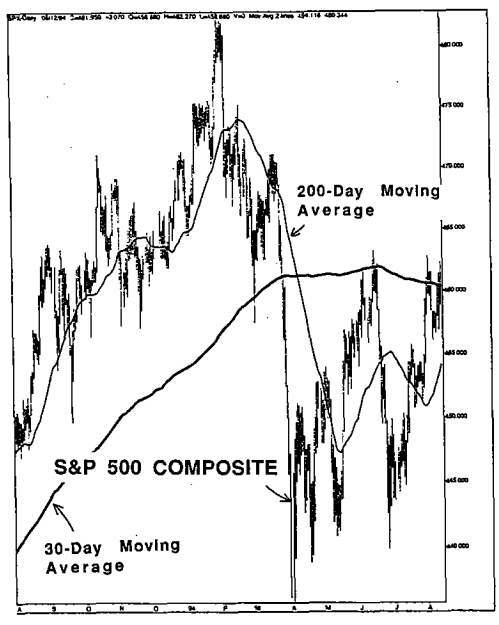
My feeling is that when the 200-day MA on the Dow finally turns down (with the 30-day MA below the 200-day MA) the bear market will be on in earnest. Reason: So far, the Dow has been the strength of the market. When the strongest segment of the market finally turns weak, the bear will be in command.

**NOTES & QUOTES:** I'm going to start this section with a very significant chart. It is an Ed Hyman (*ISI*) chart, which shows that G-7 money growth is now at a record low. This presents a huge problem, since almost every nation in the world is now either growing economically or wanting to grow.




The question -- what happens when the world is on the growth path, but the rate of money supply growth has declined to record lows? Answer: if the product (in this case, money) is scarce, then you have to pay more for it. And paying "more" means rising interest rates. However, economic growth accompanied by rising interest rates doesn't guarantee a bear market. So if the bear is to be for "real," something else has to happen. What? War? Interest rate spiral? Economic squeeze? Recession? Monetary crisis? Who knows? That's for the bear to figure out. But the chart is not fantasy, it's reality. The money just isn't there.

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Dr. Kurt Richebacher, formerly chief economist for Germany's mighty Dresdner Bank, writes in his latest report: "Having created the bubble, the Fed now seeks to gently unwind it with a policy of timid rate hikes. The effort is doomed to fail. History proves that financial bubbles can only be prevented, never cured. According to our analysis, the Fed has definitely lost control. Liquidity in the US markets and economy has become a function of monetary velocity that depends on a continuous flight of the public out of liquid money balances. That can't last. Already, despite a continuing steep yield curve, the flight from cash has sharply slowed. Once the rush for safety begins -- a so-called *"dash to cash"* -- the cataclysmic crash will inevitably arrive. Both bonds and stocks will suffer,

reverberating a crisis around the world. There is no way the Fed can prevent the crash. All it can do is try boosting the money supply -- the liquidity supply -- by adding bank reserves. But this won't work in the end." Russell comment: Dr. Richebacher believes that the Fed has created the greatest financial bubble in world history. History, says Richebacher, tells us that there's no painless way to deflate a financial bubble. We'll find out, won't we? [His FAX is (905) 957-0602.]

* *

Former Fed board member Wayne Angell (he's now chief economist for Bear Stearns) has been saying that the Fed "should" boost rates by 100 points. More recently he's been predicting that the Fed will raise rates by 50 points. But the word is that Angell is really angering the Fed with his widely-advertised interest rate forecasts. Insiders say that the last thing the Fed wants to do is fulfill Wayne Angell's predictions. Meanwhile, confusion seems to reign at the Fed. To raise or not to raise, as notes this clip from the August 4 *NY Times*. (By the way, the SEC is now investigating Angell.)

## *From Consensus to Doubt*

*Fed Is in a Quandary Over Whether to Raise Interest Rates*

By KEITH BRADSHER

Special to The New York Times

WASHINGTON, Aug. 3 — Top Federal Reserve officials are in a quandary: despite what other analysts see as signs of Economic slowing growth they day and the retail sales figures that come out next week.

Five members of the central bank's interest-rate policy committee said in separate interviews this week that unlike many Wall Street analysts, they did not see the huge increase in business inventories during also making Federal Reserve officials nervous. If they delay too long in raising short-term interest rates for the fifth time since February, they may allow inflation to rise again later this year or early next.

But what if the business community made the wrong bet on the consum-

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Last week Columbia University's Center for International Business Cycle Research confirmed that its leading inflation index rose to 189.1 in July. This was its tenth straight monthly increase. Auto prices have been increasing, housing prices are rising, and last week Chrysler accepted a 10% increase in steel prices. Hot rolled steel, the industry's benchmark, is up 40% from last year. No wonder the Fed is wringing its hands (and no wonder the bond market has been sagging).

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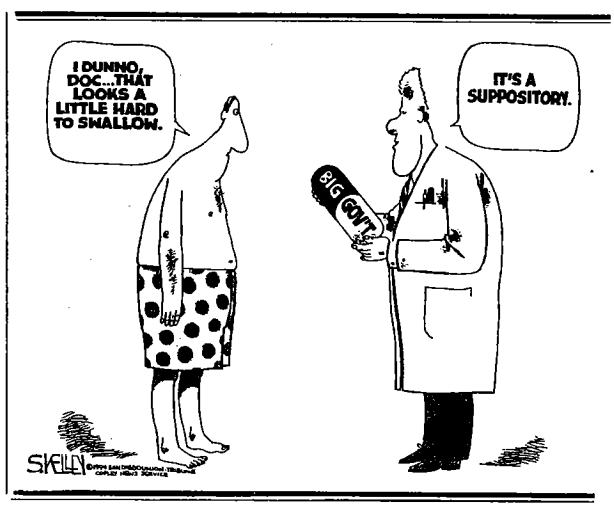
The Russell opinion regarding any government medical plan (assuming one is finally chosen): to the extent that the government runs it, it won't work. If the government runs it 100%, it will be a disaster.

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The "little stocks" are not doing well. For instance, the weighted index of San Diego's 40 most heavily-capitalized stocks has now plunged 34% from its November 10 peak. That's a lot of money lost, at least in S. California.

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Up-beat: You've got to appreciate Wayne Huizenga. How many people do you know that have started two major corporations? First Wayne started Waste Management (now WMX Technologies). Then he started Blockbuster Entertainment. Blockbuster now has 4,200 stores, and it's opening a new one every 24 hours. Wayne likes businesses that offer repeat rentals. Wayne bought the Florida Marlins (baseball). He bought the Florida Panthers (hockey). And then he bought the Miami Dolphins (football). He's the only American who owns three sports teams. Says Wayne, "I look at sports as software." And isn't that what sports are about -- renting seats game after game? The latest -- Blockbuster has bought 1,800 acres between Miami and Ft. Lauderdale, and the wags are calling the new idea "Wayne's World." It will be a sports and entertainment complex with a major league stadium, a movie studio and amusement park and golf courses (it's scheduled to open in 1998). Wayne Huizenga is only 56. And you pronounce his name HI-zenga. What next?

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No, I don't think the newly designed $100 bills are part of a government conspiracy. The new bills represent the initial part of the first re-design of US paper currency since 1929. (Mmm, fateful year -- is this a coincidence?) Washington will start with the $100 bills, then move to redesign the $50s, $20s and $10s. About half of all US currency now trades overseas, and it is thought that $1 billion or more of this paper is counterfeit. Worse, it seems that most of this junk paper is being printed by Mideast governments, although Russia could be involved as well as the Italian Mafia. At any rate, the new bills will be difficult, if not impossible, to duplicate (with all the sophisticated modern printing capabilities, it's been far too easy to counterfeit the current US money).

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Watch the Dutch. The Netherlands' PTT Post BV (post office) has opened offices in the US, Canada, Singapore, Thailand and the UK. In the past five years the Dutch PO has built a network that collects foreign mail, takes it to Amsterdam for sorting and then delivers it throughout the globe. It's the new world of international competition for mail and the Dutch are leading the parade. The Dutch PO says that its new business (started five years ago) is highly profitable. The US PO doesn't like it (what's new?), but post offices in Ireland, Canada, New Zealand and Australia have been given wide latitude from their governments to compete internationally. In the meantime, the US PO has posted a $1.7 billion deficit and is about to raise the price of a first class stamp to 32 cents. The crazy PO just gave bonuses to its 1,000 top executives! How long can the US PO with its "snail mail" survive against not only FAX and E-Mail but international competition? Your guess is as good as mine. Last call: privatize the US PO before it's too late.

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Big Mistake: Former Salomon head, John Gutfreund, was forced out of Salomon due to its Treasury bond scandal. At the time he was offered a $10 million settlement. Gutfreund didn't like the offer; instead he went to the Big Board's arbitration committee. They gave him zilch -- nothing. Furthermore he wasn't permitted to exercise 745,000 stock options he'd nominally earned since early '84. Many thought he was badly treated by Salomon. But previously Salomon had to pay $290 million to the SEC as well as hundreds of millions in legal costs. Obviously, the whole affair made Warren Buffet "mad as hell and he wasn't going to take it anymore." (Buffet was a major stockholder; after he kicked Gutfreund out, Buffet ran the company.)

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Oops, Another Mistake: Barry Diller had an option to buy 1.6 million shares of QVC from Tele-Communications at $34 a share. But Diller let the options expire on July 11 when he anticipated the completion of the CBS-QVC merger. Two days later Comcast killed the deal by making a bid of $44 for QVC. Diller suffered a loss of $15 million by allowing his options to expire. Ah, well.....

* *

Peter Cohen, former chief executive of Shearson Lehman Hutton, is on the move. He joined conservative Republic New York Corp., but he left there after two years to form a new investment firm. Says Cohen, "I see, instead of mutual funds, hedge funds as the vehicle of the future." Cohen might just know what he's talking about. Besides buying stocks, hedge funds are allowed to short the market.

* *

It seems that Joseph Jett, alone, was responsible for Kidder Peabody's phony $350 million profit in government bond trading. Incredibly, none of Jett's bosses caught the scam. Problem: the higher-ups didn't understand what Jett was doing. The mathematics were beyond them.

* *

Wall Streeters are noting that the dollar has followed the "approval-ratings path" of presidents. Strong presidents have been accompanied by a strong dollar and vice versa. Writes Kevin Phillips in the *Washington Post*, "Over the next two years, political observers can do worse than watch the currency markets. When it comes to the fate of US presidents, cynical currency traders have been right more often than not." Russell comment: Clinton unpopularity does not bode well for the dollar. But it's not what we think of Clinton, it's what the world thinks of him. At this point the world sees Clinton as indecisive, weak, hampered by a low approval rating and a very likely one-term president.

Here's another one: David Shulman, Salomon's chief market analyst, states that strong presidents make strong stock markets and vice versa. He writes that over the past 40 years bull markets have a strong correlation with monthly presidential approval ratings over 60%. Witness the rising stock market under Kennedy in the '60s and Reagan in the '80s. "Simply put, leadership counts," he adds. Noting that Clinton's approval rating is around 42%, he adds that bear markets dovetail with presidential approval ratings below 50%. Russell comment: Shulman's observations are probably true as far as the secondary trend of the market is concerned, but the primary trend is not set by presidents, Congress or Fedheads or anyone else. The primary trend is a law unto itself, and a given bull market or bear market may entail the span of two or three presidents.

* *

I bought a couple of the new PowerMacs last week. They're great, and they'll be even better when Microsoft comes out with some new software for them (promised in September and October). Each PowerMac has built-in CD-ROM capabilities: CD-ROM = "Compact Disc, Read Only Memory." I've heard that a lot of the CD-ROMs are hastily put together affairs, and according to a recent *WSJ* article, "Many of these discs are hard-pressed to deliver even a minute's worth of interesting information or entertainment." Well, I bought Microsoft's *Encarta Encyclopedia CD*, and this disc is amazing. The single disc contains the complete text of the 29-volume Funk and Wagnalls New Encyclopedia with over 1,000 new articles, thousands of photos and illustrations, bird and animal sounds, reading by authors, actual music (you can hear Louis Armstrong playing jazz, Miles Davis, Coleman Hawkins, etc., audio samples of 45 different languages, etc. (I can now say "thanks" in Swahili.) It's a huge, fascinating collection of information and entertainment -- all for $89. I liked it so much I went back and bought another *Encarta* for my younger kids. Good CD-ROMs have to be one of the waves of the future.

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High Finance: O. J. Simpson will almost surely be broke whether he wins or loses his trial. At the time of his divorce (1992) court papers valued his estate at $10.8 million, and it was estimated that Simpson was earning between $730,000 and $1 million a year. But he has put together one of the most expensive defense teams ever seen; so far, ten lawyers have appeared publicly or signed briefs for him . . . The Menendez brothers started out (following the shotgun murders of mom and dad) with their parents' assets of $14 million. As of now, their assets are down to zero, and a second trial is coming up . . . Lisa Marie and Michael -- the Presley estate is estimated to be worth $140 million; Michael Jackson is estimated to be worth $300 million. The dashing couple may face problems, but money won't be one of them.

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Imports have been flooding the shelves of US stores -- shoes from Korea, toasters from France, Hondas from Japan, the merchandise is beginning to pile up. Statistics show that inventories are now building faster than US consumers can buy them. The pile-up could be a result of the weaker dollar, a dollar which has rendered many foreign imports too expensive for Americans. Or it could hint of the peak of the expansion. Or -- well, no one knows for sure. Let's watch the stock market for the real story.

* *

The Whitewater hearings have become almost a national joke -- or an embarrassment. Even *USA Today*, which has been very impartial and fair towards the Clinton administration, ran out of patience last week. In a lead editorial, the paper growled, "Can't any Clinton official give a straight answer about Whitewater? It doesn't seem so. Not from the Senate testimony this week by top Treasury officials. Their stories clashed like polka dots and plaids as they tried to explain away White House-Treasury contact. The Administration's words and deeds have been in constant conflict. It consistently promised openness but -- (1) refused for weeks to hand over Whitewater files to the Justice Dept. (2) Balked at naming a special prosecutor. (3) Held back tax returns dealing with the Clintons' Whitewater investment." Russell comment: Day by day, week by week, the Clintons' blatant hypocrisy, manipulations and secretiveness is undermining any faith the American people have in this administration. At least we're learning to use new evasive words (courtesy of the Clintonites in front of Congress), words like "redactions," "recusals,", "staybacks," "pre-briefs" and "turnings." Ugh. Yuck.

* *

Help, they're opening coffee houses and pizza parlors all over La Jolla. The mark-up on both items is BIG. According to *USA Today*, a cup of espresso costs the purveyors eight cents, and generally sells for $1.25 to $2.00. Me, I stopped drinking any kind of coffee years ago. I find caffeine to be a very powerful drug, addictive, a "hopper-upper" and a strong diuretic. So who needs it? As for pizzas, they may be delicious, but they're full of fat (most cheeses are 50% fat). And darn it, fatless cheeses won't melt, they just soften into a sticky mess.

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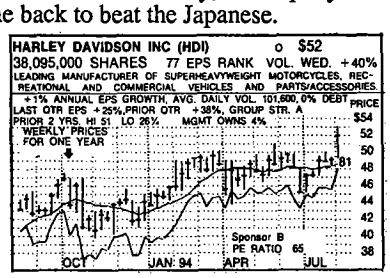
Readers must know by now that I like Harley Davidson -- the bikes and the stock. The stock hit a new record high last week at 52. Dealers have been sold out on the '94 bikes for months and are now taking orders for the '95s. Special customized bikes are in the showrooms for prices up to and above $30,000. Harley ships about one-third of their production overseas (the big Harleys are prestige items in foreign lands). Once you buy a Harley, you're also a buyer for parts and extras, and they can add up fast. Harley, the great American success story, a company that was down and out, then came back to beat the Japanese.

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While on the beach last week I dreamed up this strange interview. "Where were you born?" "Pango Pango." "Where do you live now?" "Walla Walla." "Mmmm, where do you work?" "At the UN as assistant to Boutros Boutros-Ghali." "Any hobbies?" "Yes, I play cello with Yo Yo Ma." "Is your mother living?" "No, she was killed in Africa by the Mau Mau." "How about your father?" "He's doing time in Sing Sing." "I see that you're married; what's your wife's name?" "LuLu, she's a night club dancer." "Does she do the Go Go?" "No, the Can Can." "What's your favorite food?" "Bon Bons." "Not very nourishing; how's your health?" "I have beri beri." "You know something, I'm very much afraid you're coo coo."

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The Last Guru: Smith Barney star Elaine Garzarelli's fund underperformed the S&P in five of the last six years, so her fund's being folded into SB Strategic Investors Fund. *Morningstar* called her "a one hit wonder." That's mean. Russell adage: "There are no geniuses on Wall Street, only geniuses for a while."

* *

*Time* magazine (not too surprisingly) has turned against Clinton or at least his morals and his programs. More surprisingly, *Newsweek* has now turned against the Prez, with the latest issue giving a thorough thumping of Clinton's "universal health plan." Last week Congress, in a shocker, gave the thumbs down to Clinton's $33 billion so-called "crime bill" (which many term more of a make-work pork bill). With the crime bill sidetracked or finished, if no health bill is passed, the Clintonites will be completely demoralized, if they are not already. The fact is that Clinton wants more entitlements, more government takeover, but the growing sentiment is LESS entitlements, less government, less

debt and I guess, less of almost everything Clinton and Hillary stand for.

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The Big Count: Dems now control the Senate 56-44 and the House 256-178-1. Only twice in this century has the party in power not lost Congressional seats in an off-year election. A typical off-year (including some Dem losses) would give Dems a very tenuous hold on Congress, but it would give Clinton an even tougher time passing his legislature. However, a Dem disaster -- say a loss of five to seven Senate seats and 30-40 House seats -- would leave the Clintonites with the least control of any Dem administration in memory. And that's exactly the message the Republicans want to send to the American people. As I see it, the vote this Fall is going to be basically a vote for or against the Clinton administration, much more than a vote for Republicans vs. Democrats.

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In a dire report sent to Clinton by the *Bipartisan Commission on Entitlements and Tax Reform,* the conclusion was that by the year 2012, entitlements and interest on the national debt will consume ALL federal tax revenue. This report was not put out by a bunch of kill-joy nuts, it was the product of a presidentially appointed commission. Here's what else the report said. Expenditures for Medicare and Medicaid will triple as a percentage of the economy by 2029. Social Security funds will be depleted by 2029. The Medicare Trust Fund will be empty by 2001. Russell comment: Expect major cutbacks in entitlements within the next five years. Furthermore, expect an entitlement backlash -- anger and gnashing of teeth as the American people finally realize that the government has promised and committed itself to far more than it can pay for. I expect that the next political-social wave will be a massive swing back to conservatism (all of this could dovetail with the major bear market that I see ahead).

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This is from columnist George Will: "The most interesting argument in America in the 1990s is going to be whether or not the attempt to build all this security into life has changed the American character. That is what the welfare argument is about, that is what the argument over illegitimacy is about -- the feedback effect. There is a wonderful new book out called, *'Dead Right'* by David Frum. He says that if you have a big government, which takes the risk out of life, you are going to take away the Americana character that grew up when life was full of risks. If you got pregnant when you were unmarried, that was risky, because there was a stigma attached to it. One of the reasons why there is no stigma attached to it now is because the government is there. Frum says that the paradigm of the welfare state is this -- because people feel more secure, they engage in risky behavior." Russell comment: I agree -- you won't have to work, you don't have to be married to have a baby, you don't have to plan for the future, because the government will take care of you.

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Odds 'n Ends: I've got to be more careful about what I write. After my last Letter I received a lot of correspondence from worried subscribers -- many thought I was preparing to "check out," preparing to go to that great analysts' chart room in the sky. Nothing could be further than the truth. Honest, I was just reminiscing. I intend to be writing into my '90s (my super-gene mother lived to be 92, then got extremely bored and willed herself to heaven). All of which means you may have to put up with me for another 20 years or more . . . Got a letter today from hard-money icon Gary North who writes,*"You World War II guys are a breed apart. You won the big one (I write this on the 49th anniversary of the Nagasaki bomb)."* You know it's strange, I sometimes feel like I have one foot in history (was I really bombing the Brenner Pass?) and the other foot in the future (hey, wonder which way is the market heading?). But face it, Russell, you can only exist in the present -- any psychiatrist will tell you that . . . We're having a heat wave in S. Calif.; and when it's 90 degrees where I live (just 100 yards from the beach,) you know it's HOT! .... Paul Penna visited me last week. Paul is president of Agnico-Eagle Gold Mines, and he's highly optimistic about his operation (which he should be, since it's a real growth situation). Paul's one of the old-timers in the gold industry, and he's a travelin' man; told me he recently visited with Harry Schultz in Monaco (Harry's my son Ryan's godfather) and notes that Harry needs to put on some weight -- listen up, Harry!) . . . Also received a visit from Marc Faber, *Barron's* expert on Asia. Marc writes the *Doom, Gloom and Boom Report* out of Hong Kong. I hadn't met Marc before, and for some reason I was expecting a very conservative-looking gentleman. I told him I'd be on my motorcycle, since parking a car in La Jolla at mid-day isn't easy. I found Marc replete with a chamois vest and pony-tail. My kinda guy.

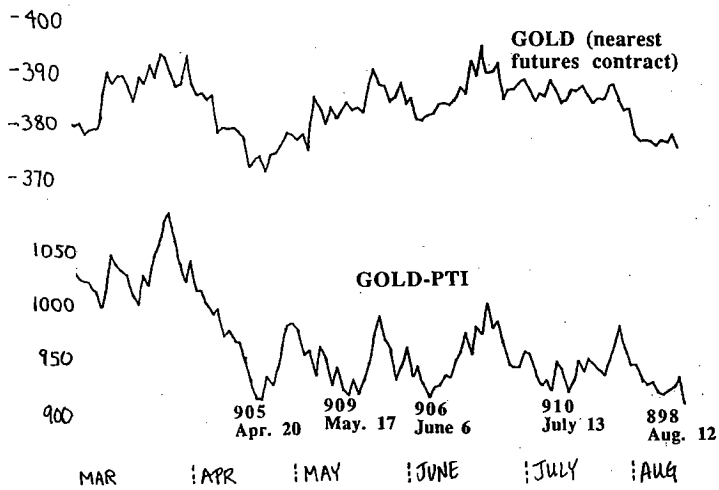
**GOLD:** Four times my Gold-Primary Trend Index (G-PTI) has sunk into the area between 905 and 910, and each time it bounced off those lows and rallied. On August 12, however, the G-PTI broke below the 900 level for the first time.

Is this the signal for a generally lower level for the whole gold spectrum? Or is it a final false move calculated to wash out the last remaining hopefuls? There's simply no way of knowing. Gold, it would seem, is bargain-priced at these levels. Platinum (spurred mainly by rising demand) has been strong. Silver is weak, barely holding above the $5 level. And interest rates, globally, are gradually rising, making it increasingly attractive to hold the currencies.

My point & figure chart of gold shows a secondary sell signal when gold hit 380. But gold is still holding well above its rising trendline. There's support at the 374 level, but another and stronger sell signal would come if spot gold (second London fix) hits 370.

Meanwhile, almost every variety of economist is telling us that there's no current inflation and no inflation in sight. One could almost take a contrary opinion on that one. To add to the confusion is the world money picture. The growth of the G-7 (i.e., seven leading industrialized nations) money supply has hit an all-time low (see chart in Notes & Quotes section). Can we have inflation with this kind of declining money growth? But how long will the central banks stand for low money growth?

Questions Questions: what are we looking at -- world deflation? Or are we looking at the very early stages of world re-flation? If this is a bear market in stocks and if money supply growth continues to contract, I would have to bet on world deflation. And if that occurs, could the US financial system (with its **$15.9 trillion** in built-in debt) hold together? And if the US financial system cannot hold together, then what's a dollar worth?




**Late Notes:** The same old (continuing) story: Transports are lagging behind the Dow, daily advances and declines are almost equal regardless of what the Dow is doing (implying "churning,") daily new lows are running above daily new highs, and individual stocks swoon on any kind of bad news. I note that almost all the closed-end funds from A to Z, from the Asia Pacific Fund to the Zweig Total Return Fund, are breaking down. Any premiums are being squeezed out of these funds, and the funds are dropping behind the market in performance. The plush days of Wall Street are slowly but relentlessly drawing to a close. And the bear's grip is tightening, slowly, ever so slowly. . . Joe Granville's latest shocking count -- 670 NYSE stocks now within one point of 52-week lows.

NEXT MAILING: Aug. 31, 1994